

COVERING CONFIDENTIAL



Foreign and Commonwealth Office

London SW1A 2AH

13 May 1988

N L Wicks Esq CBE
10 Downing Street

Dear Nigel,

TORONTO ECONOMIC SUMMIT: THIRD SHERPAS' MEETING

1. I attach briefing for the next meeting of Personal Representatives. It consists of:-

- 1) Steering brief
- 2) Comments on the Thematic Paper Subject briefs
- 3) World Economy
- 4) Developing country issues (debt and aid)
- 5) NICs
- 6) Uruguay Round
- 7) Structural Reform (including Financial Markets)
- 8) Agriculture
- 9) International Investment
- 10) Political issues
- 11) Possible UK and other initiatives

2. The subject briefs are those provided for Ministers attending the OECD Ministerial Council, with additional points to make: Geoffrey Littler and I will be able to bring you up to date on the outcome of the Council meeting.

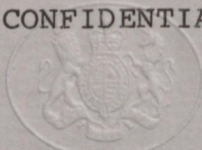
3. I also attach a copy of the programme for this meeting, sent to us by the Canadian High Commission; you may already have a copy.

*Yours ever,
Rodric*

R Q Braithwaite

Copy Sir G Littler KCB

COVERING CONFIDENTIAL



THIRD MEETING OF PERSONAL REPRESENTATIVES,
19-21 MAY

BRIEF NO 1: STEERING BRIEF

1. Mrs Ostry's letter of 9 May sets out the agenda for this third meeting, the main purpose of which is to take the Canadian thematic paper. It will not survive in its present form but no doubt the Canadians intend it to serve as a quarry for communique language.
2. Dinner on 19 May will be devoted to a review of recent developments. Sir G Littler and Mr Braithwaite will brief you on the outcome of the OECD Ministerial. The draft communiqué (as of 12 May) is attached: the trade and agriculture sections are still full of square brackets.
3. Sherpas will discuss ancillary issues over lunch on 20 May. On the number of Summit texts, we are sticking to one economic and one (selective) political communiqué.
4. Presumably Mrs Ostry will also want to discuss new initiatives and topics for the informal discussion on the first full day of the Summit. The two tend to shade into one another. We want to send a firm message on the strengthening of GATT as an institution; take forward work on terrorism; and possibly suggest informal discussion among leaders of health care in the '90s. The first of these can reasonably be worked into discussion of the economic text (Uruguay Round issues); the second is really a political topic (see Brief No 10). We might also put in a small plug for a reference to AIDS in the communique. We have provided defensive (but reasonably positive) lines to take on potential initiatives from others: environment (Italy; Canada; possibly FRG and US too); drugs (much on the minds of the Americans); and the Japanese Human Frontier Science Programme (HFSP). Brief No 11 gives essential information.
5. Over dinner on 20 May there will be a tour de table on political issues. We want leaders to concentrate on East/West, Middle East and terrorism. But the Canadians seem to want only East West, and



are trying to make discussion of other issues conditional on discussion of South Africa, which we continue to resist (see Brief No 10). The latest report from Ottawa says that Mr Clark still wants a discussion of South Africa.

6. Mrs Ostry will probably want to work through the thematic paper: we have provided a page by page commentary (see Brief No 2). You might like to focus your colleagues' attention on a possible theme for the next stage of drafting: the communique itself. As Sir Geoffrey Littler suggested, an appropriate theme might be an overview of this second 7-year cycle of Summits, which would allow many of the participants at Toronto to claim (personal) credit for the achievements since the Versailles Summit of 1982. An upbeat theme like this would also usefully counteract the warnings of imminent doom which tend to characterise Mrs Ostry's treatment of macroeconomic issues.

7. The outcome of the OECD Ministerial is of course as yet unknown: your subject briefs nos 3-9 are based on the material provided for Ministers. The two issues of most concern to us are agriculture and trade (particularly the Uruguay Round Mid Term Meeting (MTM) to take place in Montreal this December). On trade (principally dealt with in paras 26 and 30-35 of the thematic paper), Summit leaders will want to put their political weight behind a successful outcome to the Uruguay Round. We would prefer alternative wording on the MTM in paragraph 35 (see brief no 2). Canadian ideas on the role of the GATT are in paragraph 31; this would be one opportunity to press the Prime Minister's concerns. The key paragraph on agriculture is 34: it goes unrealistically far by implying that the Summit would be able to agree on a target depth of cut in support. We may not even get that far at the MTM in December.

8. We shall provide briefing nearer the time on latest developments over the Chancellor's debt initiative (paragraph 44). The Chancellor will discuss tactics with Mr Wilson of Canada on 16 May.

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Canadian High Commission



Haut Commissariat du Canada

May 9, 1988

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10 MAY 1988	

Dear Colleague

It occurs to me that you would find it useful to know something further of our planning for the Third and Fourth Sherpa meetings in terms of their call on your time and schedules.

As outlined in my letter of 26 April, the Third Sherpa meeting in Paris will start on 19 May in the evening with a reception followed by separate dinners at the residence of the Canadian Ambassador in Paris. Sherpas would, if you agree, discuss recent developments and their relationship to the Summit. These would include the OECD Ministerial and other recent meetings as well as an indication from the French Sherpa of the likely priorities of the new French government. On May 20, plenary sessions at the Centre Kleber would be devoted to discussion of the thematic paper, while over lunch I believe Sherpas should discuss ancillary issues as well as the nature, length and number of Summit texts we would like to see come from the Toronto Summit. We will also provide a short update briefing on Summit logistics that afternoon. At dinner, once again at the residence of the Canadian Ambassador, we might engage in a tour de table on political issues. On the morning of 21 May, at Centre Kleber, we should attempt to sum up. I have made no plans for continuing this meeting over lunch as many of us will be anxious to return to our capitals as soon as possible.

As you will recall, after much consultation, we decided to stick to our original plan of holding the Fourth Sherpa meeting at the Millcroft Inn outside Toronto, June 3-5. Political Directors will meet in Toronto June 4 and join us for dinner that evening. My proposal for this last meeting would be that we tackle new developments at our dinner opening June 3, devote plenaries on June 4 to the main Summit economic text, with luncheon discussion among Sherpas given over to ancillary issues and other possible texts. That evening, with Political Directors, we would map out a strategy for addressing political issues at the Summit and discuss possible political Summit language. On June 5 we would sum up on economic issues in the morning plenary, and then, over lunch, revert to political issues among Sherpas alone to discuss how we might integrate our conclusions with the

Political Directors into Summit planning as a whole. Because of the inability of Political Directors to meet with Sherpas until 4 June, I fear that there is no way of avoiding a lunch among Sherpas on 5 June. In the afternoon we would propose a visit to the Toronto Summit sites, with departures for capitals in the early evening. I trust that these plans can be accommodated at this last, and most important, of our Sherpa meetings prior to the Toronto Summit.

For those returning to Europe, nearly all flights to Europe leave in the early evening so that members of our group who need to be at meetings in Luxembourg in the morning of 6 June should be able to get there on time (eg KLM flight KL692 departing Toronto 1725 arriving Amsterdam 0630 connects with flight WU205 departing Amsterdam 0850 and arriving Luxembourg 0955).

Please let me know if you foresee any problems with these scenarios for our meetings. I look forward to seeing you later this month in Paris.

Yours sincerely

SYLVIA OSTRY

Mr Nigel Wicks, CBE
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to the Prime Minister
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6 May 1988

TORONTO ECONOMIC SUMMIT
THEMATIC PAPER

Developments since Venice

1. The Summit countries are now in their sixth consecutive year of economic expansion. Output growth in the past year has, on average, been stronger than expected. Unemployment rates fell markedly in North America and the United Kingdom -- where the pace of expansion exceeded potential growth -- but were either unchanged or increased in other Summit countries. Unemployment remains high in a number of countries, especially in Europe.
2. Inflation has been restrained. Nevertheless, recent developments in some countries have engendered concerns about a resurgence of inflationary pressures. Interest rates generally have declined, particularly since October, equity markets have recovered, and tensions in foreign exchange markets have eased. (A)
3. Progress has been made toward the correction of external imbalances. The real trade balances of the three major economies have adjusted considerably toward more sustainable positions, although in US dollar terms current account deficits and surpluses remain large. The realignment of exchange rates in the past three years has contributed to the international adjustment process. So have the measures to stimulate domestic demand in surplus countries and reduce it in deficit countries. Fiscal consolidation has proceeded in countries with high fiscal deficits.
4. Over the past years, economic policy coordination among the Summit countries has been intensified and strengthened. Countries have agreed on the basic orientation of their policies and have made specific commitments to reach those aims, as demonstrated especially by the Louvre Accord and last December's Group of Seven statement. Substantial progress has been made in attaining the agreed policy objectives.
5. Nevertheless, financial markets have remained concerned about the persistent large international imbalances. These concerns were underscored by the late-October stock market turmoil and the subsequent foreign exchange market turbulence. Although a substantial degree of calm has been restored to financial markets, and although the October stock market plunge does not seem to have (B)

This should be put in a positive way

Developments
Since Venice

Develop
SINCE
VENICE

+ Too gloomy, too much
alarm A+B+C.

+ There is more to be done
see OECD Comynge

PARA NO:

1. Communique should not say that UK expansion exceeded potential growth.

2. Communique should not dwell on concerns (though they certainly exist, cf EPC meeting) about a resurgence of inflationary pressures - should instead reaffirm common objective of achieving low inflation.

3. Second sentence. Disagree with use of 'in US dollar terms' (not the best way of measuring imbalances). Strictly, the last sentence should say 'some' or possibly 'most' countries.

5. This is very unhelpful. It is important that communique avoids such alarmism. In particular, [see over]
/communique

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A bit scary

(c)

significantly undermined consumer and business confidence, the risk of renewed turmoil in the months ahead cannot be excluded should the adjustment process appear to falter. Expectations and market confidence remain fragile.

6. To lessen the vulnerability of the world economy to turbulence in financial markets and defuse tension in the international trade and payments systems, governments must reinforce their commitment to the goals of sustainable economic performance and external positions. Government policies must be seen as credible in addressing those goals. Commitment and credibility will restore market confidence.
7. In the developing countries growth weakened in 1987, but the terms of trade recovered and, on aggregate, debt-export ratios declined for the first time since debt problems became acute in 1982. On a regional basis, however, divergence in performance intensified. The Asian economies continued to grow strongly, whereas the Latin American economies weakened considerably. Growth in Africa remained feeble.

Policy Coordination : Macroeconomic Policies and Exchange Rates

8. The foremost policy challenge facing Summit-country governments is to manage the transition over the medium term to more sustainable economic and financial positions in the context of non-inflationary growth. To meet the challenge, governments should firmly follow the agreed strategy of coordinated efforts to reduce spending in countries with large external deficits and stimulate domestic demand in countries with large external surpluses.
9. The reduction of external imbalances will require the cooperation of the Summit countries, of newly industrialized countries with rapidly growing external surpluses, and of some of the smaller European economies.
10. External imbalances have their counterpart in national saving-investment imbalances. For the past several years, private saving in the United States has been insufficient to finance the sum of domestic private investment and government deficits. Continued efforts to increase US private and national saving would contribute to the adjustment of international imbalances. Recent indications that the declining trend in private saving may have bottomed out are encouraging. In contrast to the situation in the United States, national savings in Japan and Germany have exceeded domestic investment.

We really should say there is a need to reduce further US deficits

But these means further action

Policy
Coordination

POLICY
COORDINATION
POLICY
EXCHANGE
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communique must avoid speculative references to 'renewed turmoil in the months ahead' on the stock markets, and to market confidence remaining 'fragile'.

8. An example of the tendency towards demand management language, eg for 'stimulate' (penultimate line) substitute 'ensure adequate growth of'.

Further action is required

9. (see also paras 27-9 on Asian NICs). US will probably want reference to NIEs ('economies') rather than NICs (countries), to include Taiwan and Hong Kong - as per G7 communique.

✓ 10. What are the efforts to increase US private saving referred to in the third sentence? The paragraph contributes little beyond stating a necessary national accounting identity.

Obviously, but what action?

11. Over time, as the U.S. federal government deficit is reduced, an increased level of national saving will be available to finance U.S. private domestic investment. It will be essential, therefore, to ensure that the savings the United States has been absorbing from the surplus countries find alternative productive outlets in order that world economic growth be sustained. For instance, the "excess" savings in the surplus countries could finance increased public investment (e.g., in infrastructure and human capital) or reductions in taxes that encourage increased private spending in the surplus countries themselves. Alternatively, the savings could be transferred to other countries, in particular to developing countries. However, given the reluctance of the private sector to invest in many developing countries, a transfer of savings to those countries would require an increase in official capital flows or incentives to private investors. In this respect, Japan's efforts to recycle part of its current account surplus to developing countries are encouraging.

Need to
mechanistic
approach.

Implications?

12. At the Tokyo and Venice Summits and with effective use of the G-7 forum, the Summit countries have developed and strengthened the process of greater policy coordination. The process involves both the use of indicators in multilateral surveillance and an intensified system of consultation. The Summit itself serves as a forum for reviewing the progress made. In this respect, the efforts being made to refine the analytical use of indicators and possibly augment the existing set by the inclusion of a commodity-prices indicator are welcome. Summit countries should reaffirm their commitment to improved and effective policy cooperation.

of course.

13. The adjustment of international imbalances underway involves a shift of resources across sectors. In bringing about this shift, three factors play a role: exchange rates, expenditures, and structural flexibility.

14. The large exchange rate changes in the past three years, in particular the real depreciation of the U.S. dollar against the Japanese yen and the major European currencies, have played a major role in the adjustment of real trade balances experienced so far. The shifts in international competitiveness achieved should continue for a time to move external positions toward more sustainable levels. Under present circumstances, further large exchange rate changes would not serve the adjustment process.

OK, but how do we stop changes!



11. The first three sentences are unhelpful. They give support to fiscal expansionists who would stress the danger of world recession as the US adjusts. The suggestion that surplus countries should transfer 'excess' savings to LDCs seems to point the finger at Germany, given the acknowledgement of Japanese efforts in the final sentence.

*Aimed too mechanistic approach.
The world is not like this.*

12. We would wish in the communique to play down the indicator exercise and would hope that the Summit will not on this occasion spend much time on this.

No || 12 & 14. A reference to exchange rate stability as an objective of policy cooperation is necessary; paragraph 14 could also do with being less grudging on this point. Concerned that these passages do not sufficiently reflect the Chancellor's concern to highlight the objective of exchange rate stability within a non-inflationary policy stance.

15. Exchange rate changes alone, however, are not sufficient to bring about the desired adjustment of external imbalances. Changes in expenditures are also necessary; especially reductions in the rate of growth of private and public consumption in the deficit countries and increased domestic investment in the surplus countries. Without accompanying changes in relative levels of domestic demand across countries there would likely be continuing pressures on exchange rates. In the event, exchange rate changes could be counterproductive: capacity and demand constraints could translate the exchange rate changes into higher inflation in the depreciating countries and deflation in the appreciating countries.
16. The Summit countries have undertaken a series of fiscal and structural measures to bring about the required adjustments. Efforts in those directions must continue if the progress to date is to be sustained. The focus of markets is on continuing coordinated efforts to correct the imbalances; the expectation that appropriate fiscal actions will be taken within a medium-term framework is essential to underpin the market confidence necessary to maintain exchange rate stability.
17. Monetary policy in the summit countries has actively supported international policy coordination. But on occasion it may have been overburdened by being asked to simultaneously achieve a number of objectives: sustain growth, control inflationary pressures, and stabilize exchange rates. A potential conflict between exchange rate stabilization and domestic monetary objectives persists. It is imperative that other policies play a greater role if non-inflationary growth is to be sustained in a context of stable exchange rates.

||| *ce*
Non
needs to
be done.

Means

Structural Policies

18. Structural policies are especially important at this juncture. By removing impediments to the effective working of market forces they would facilitate the sectoral adjustments associated with technological and demographic change as well as with the continuing correction of international imbalances. In so doing, they would help stem the tendency for protectionist pressures to shift as current accounts turn around. Moreover, a more efficient use of existing production possibilities would permit faster growth. This is all the more important in countries where available spare capacity is a constraint on non-inflationary growth, and especially

Structural
Policies

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15. The first sentence is ambiguous in that it might seem to suggest a role for future exchange rate changes.

15-16. Usual FRG problems on fiscal stimulus?

17. What are the 'other policies' referred to in the last sentence? Could it indicate more clearly that it means structural policies?

18. What does the third sentence mean? The fifth sentence is poorly drafted. Presumably what is meant is that there is a problem of structural unemployment.

where the lack of productive capacity may be associated with high levels of unemployment, as in a number of European countries.

19. Summit countries have identified a number of priority areas in which structural reforms will be pursued. These consist of further tax reforms to enhance the efficiency of the tax system and to provide incentives to work, to save, and to invest; the elimination of wasteful subsidies; the deregulation of markets and the enhancement of competition and price flexibility; the reform of agricultural policies; and the removal of trade barriers.
20. In present circumstances, structural policies to complement macroeconomic policies are particularly called for in Europe, in order to spur job creation and to realize Europe's growth potential, and in Japan, so as to support the greater reliance on domestic demand-led growth. For instance, in Europe desirable structural reforms would include further liberalization of the transport and telecommunications sectors, elimination of wasteful industrial subsidies, and removal of impediments to labour mobility. Especially important for catalyzing significant structural reform and growth is the programme to complete the European Community internal market in 1992.
21. Japan could undertake to reform agricultural support and competition policies, reform policies pertaining to the use and taxation of land, and further liberalize its distribution system and transport sector. As for the other Summit countries, the most promising areas of structural reform in Canada would be implementation of the Free Trade Agreement with the United States, further tax reform, and the proposed liberalization of the financial services sector. For the United States, a priority would be to undertake reforms that would increase incentives to save. - what
22. Summit countries should pay special attention to those areas where international cooperation may spur structural reform and contributes to the full realization of its benefits. In the area of subsidies to industry, Summit countries should encourage the work at the OECD to identify and estimate government subsidies on an internationally comparable basis and assess their impacts, so as to encourage cooperative measures for the reduction or elimination of wasteful subsidies. More generally, Summit countries should welcome the further development of the OECD's surveillance of structural reform. Means



20. Add tax reforms, where appropriate? And would we mind a further reference to reform of agriculture in the European context of this paragraph? (It is mentioned as a Japanese objective in para 21). No explicit reference to FRG's possible contribution, but may be hard to secure although the draft OECD communique contains possible language.

21. Add tax reform for Japan (which had no objection in the OECD communique discussions). Last sentence. What are these reforms?

22. As regards the measurement of industrial subsidies (a PSE-equivalent) DTI have no objection to the Summit giving a push to the work in OECD. It may be worth making a point that we do not believe that the results will be useful for the Uruguay Round (cf the time needed to develop PSEs for agriculture). But as a longer term exercise clearly it is worth developing a basis for the comparison of the impact of Government subsidies. The basis will have to be more complex than that proposed by the Australians in their ERA concept. (Energy may have problems, however, over applying PSEs techniques to their field, notably coal.)

- We could strengthen last sentence, eg "pledge their full support for"

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23. Financial markets free of distorting controls are essential for channelling funds to their most productive uses. Financial and technological innovations are rapidly integrating financial markets internationally. This entails both benefits -- a better allocation of capital -- and new risks -- in particular, the risk that developments in one country are more quickly, and fully, transmitted to other countries. The global integration of financial markets also complicates the supervisory task of regulatory authorities. Summit countries should cooperate in the examination of issues pertaining to the supervision of securities markets. *(continue to)*
24. The governments of all Summit countries have undertaken, or will be pursuing, tax reform to render the tax system more equitable, remove distortions, and reduce disparities across countries in the taxation of various forms of income. With the increasing international integration of markets, differences in national tax systems assume a greater role in individuals' and businesses' investment decisions. Governments should continue to examine ways of removing discrepancies in national tax systems which distort incentives.
25. Governments recognize the very high costs which agricultural support policies are exacting in terms of budgetary outlays, high prices to consumers, and foregone output because of misallocation of resources; and their deleterious effect on a number of developing countries, including some highly-indebted ones. Reform of agricultural policies is a high priority of Summit countries in the Uruguay Round of trade negotiations.
26. To realize fully the benefits of national microeconomic policies to liberalize markets and enhance competition, it is crucial that an open international trading system be maintained. International competitive pressures improve the political climate for domestic structural adjustment. Thus, a successful Uruguay Round is of critical importance.

Asian NICs

27. The international integration of goods and financial markets and the rapid diffusion of new technologies have been changing the pattern of international specialization of production. Certain newly-industrializing economies, in particular the Asian NICs -- Korea, Taiwan, Singapore and Hong Kong -- have become increasingly important in world trade in manufactures.

Asian
NICs

ASIA
NICs



23. We would support the proposal in the last sentence provided that it does not imply setting up new machinery. But it needs to be more fully elaborated before we commit ourselves. How do the Canadians propose that this should be carried out?

24. The final sentence is unwelcome in view of the debate over tax approximation within the EC.

25-6. We shall want to try to go further in the Summit communique. But hard to judge prospects until after OECD Ministerial. See also paras 31-5.

27-9. All good stuff but we need to be careful about the use of the word "integration" which is acquiring a particular meaning in the Uruguay Round context.

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28. Although the Asian NICs differ in many important respects, they are all characterized by dynamic, export-led growth which has allowed them to triple their share of world trade (both exports and imports) since 1960. In recent years these economies have evolved as major net exporters to the United States and net importers from Japan. But whereas in the case of Singapore and Hong Kong overall export growth has been broadly commensurate with import growth, Taiwan and Korea are now running sizeable current account surpluses. These surpluses are projected to decline only gradually in the next few years. Another Asian group, Malaysia, Thailand and Indonesia, termed the Newly Exporting Countries (NECs), are beginning to emerge as rapidly-growing exporters of manufacturers. There is a discernible trend to increasing integration by means of investment and trade flows within the dynamic East Asian region.
29. With increased economic importance come greater international responsibilities and a strong mutual interest in enhanced cooperation. In view of their growing importance in the world economy, there is a need for improved constructive dialogue between the industrialized countries and the Asian NICs, as well as the other outward-oriented countries in the region, on the international cooperative efforts required to achieve sustainable international adjustment. The development of informal processes which would facilitate multilateral discussions of issues of mutual concern, such as exchange rate and macro-policies, trade and structural adjustment policies, should be encouraged.

Multilateral Trading System

30. The multilateral trading system is fragile. Countries must continue to resist protectionism and the temptation to strike bilateral agreements outside the framework of GATT rules, and by making greater efforts to liberalize long standing trade restrictions. A successful Uruguay Round will invigorate the multilateral system and ensure its integrity, so that free and fair trade can once again become the engine of world growth. The Mid-Term Review in Montreal in December 1988 will provide a unique opportunity to send a positive political signal to the trading world.
31. To ensure this opportunity is not missed, Summit countries could draw attention to their ongoing concerns about improving the functioning of the GATT. This would be an important step to ensuring that protectionist pressures

Multilateral
trading system

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28. Makes a helpful distinction, which we should support, between Taiwan/Korea and Singapore/Hong Kong. We should try to insert a comment on the need for Taiwan and Korea to adjust.

29. We need to be cautious about 'multilateral discussions' if this means treating the Asian NICs plus other emerging NICs as a group. Obvious problems over Taiwan and Hong Kong participation. But we must bear in mind that, within the Uruguay Round, for certain purposes we may need to decide that the NICs/NIEs do constitute a group (eg in terms of the applicability of Article XII).

are resisted and the liberalization of trade in goods and services achieved by the Uruguay Round is secured and enhanced. Attention could be drawn to the need to make the GATT a dynamic organization able to assume a lead role on a range of trade policy issues, in addition to a strengthened and reinforced contractual agreement. That would involve both giving Ministers a greater role in providing guidance to GATT, as well as improving linkages among GATT, the IMF and the World Bank. As a first step in that direction, Summit Countries could make a commitment to greater transparency by allowing GATT surveillance of all trade policies. It would also be necessary to emphasize the importance of strengthening the GATT dispute settlement system.

32. A major political and institutional consideration is the future role of developing and newly industrialized countries in the GATT system. These countries (especially the NICs), should be encouraged to undertake increased commitments and obligations and a greater role in the GATT, commensurate with their importance in international trade, the international adjustment process and their respective stages of development. Equally, developed countries should consider what they are prepared to do to meet the legitimate need of developing countries for greater, more secure access for their exports.
33. Reflecting the clear terms of reference provided by the Punta Declaration and the political impetus provided by the 1987 OECD Ministerial and the Venice Economic Summit, good progress was made during 1987 in the Uruguay Round negotiations on agriculture with the tabling of major proposals. However, this promising start now faces the difficult task of moving the negotiations themselves forward. The Summit should provide fresh political impetus and support to reinforce the efforts at domestic reform by advancing the process of agricultural trade reform and liberalization in the multi-country, multi-commodity context of the GATT round.
34. The clear policy challenge for the negotiators is to develop by the time of the Mid-Term Review the core elements of a framework which would include long-term and short-term components and improved GATT rules and disciplines for agricultural trade. The prime objective of the framework would be to make the agricultural sector more responsive to market signals. This would be facilitated by agreement on the measures to be included and the target depth of cut in the aggregate level of support and protection. Any short-term measures to



31. The ideas on the role of GATT are particularly Canadian ones. We wish to preserve the nature of the organisation as a rules-based body and not turn it into a political forum addressing the world on trade policy matters. Subject to that understanding, the paragraph is not objectionable. We are also generally in favour of improving the linkages between GATT and the IFIs. However, we are not sure that it will be possible to reach agreement on how this should be achieved by the MTM. (There are pitfalls to be avoided - eg LDC suspicion of cross-conditionality. Need to proceed carefully.) Proposals on Ministerial involvement, surveillance and dispute settlement are far more advanced. (See brief.)

32. The developing countries would not find the last sentence an impressive or reassuring commitment. (See brief.) There is no harm in recognising the legitimate interests of the developing countries in the Uruguay Round and the need for a balanced outcome of benefit to all participants.

33-5. See general comment on paras 25-6 above.

34. We should certainly like a reference in the Summit communique to 'agreement on the measures to be included' (ie types of support and maybe commodity coverage), but can expect French/FRG resistance. We do not believe that the Summit will be able to agree on language of 'the target depth of cut' (ie what percentage of reduction of PSE); the MTM itself may not even get that far. This will have to be a matter for the subsequent negotiations in GATT. The last sentence is a sop to the Japanese. But has anyone thought through the implications? It sounds like an IEA-type agreement for food.

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prevent agricultural trade distortions from becoming worse would need to be consistent with long-term goals. Concerns about food security could be met by exploring ways of sharing in times of severe or unanticipated scarcity.

35. At Punta del Este Ministers committed themselves to further trade liberalization across the wide range of goods and services including such new areas as TRIPS and TRIMS. The Mid-Term Review will take stock of progress in all negotiating groups, lay out the course for negotiations to conclude the Uruguay Round by 1990 and approve a package of interim measures across a broad front. This will provide confidence building signals about the Uruguay Round and the longer-term stability of the trading system.

Developing Countries and Debt

Middle-Income Countries

36. The strategy that has been followed since 1982 in dealing with the debt problems of the highly indebted middle-income countries has met with some measure of success:
- the risk to the international financial system from the large exposure of commercial banks to countries experiencing debt-servicing difficulties has been greatly lessened as banks strengthened their financial positions;
 - many indebted countries have begun a process of macroeconomic adjustment and structural reform which is necessary for a long-run resolution of the problem;
 - lending from official sources has continued to grow at a significant rate;
 - the 'menu approach' has continued to expand.
37. Progress toward a lasting solution, however, has been slower than earlier expected. Debt ratios remain high and the return to creditworthiness for many remains in the distant future.
38. The current market-oriented, growth-led strategy which takes into account the diverse situations of different groups of countries remains the only viable strategy. The central element of this strategy is the adoption of comprehensive macroeconomic and structural reforms by the

Developing
Countries
and debt

Middle
income countries

DEVELOPING
COUNTRIES
AND
MIDDLE
INCOME
COUNTRIES



Para 35. We have no difficulty with this paragraph except that "a package of interim measures across a broad front" is compressing the idea of achieving specific agreements or results with that of "globality". It would be better to say that we should achieve specific interim agreements or measures where possible (ie institutional questions, tropical products etc); settle a framework of principles for negotiation on new issues such as agriculture, services and intellectual property; and register progress across a broad front in other areas. This will, of course, give the French apoplexy (possibly FRG and Italy too) but it might be less fatal than the Canadian formulation which implies a far more ambitious target. The US will want to go into greater detail on each aspect of the trade negotiations.

Para 38. Interest rates: distinguish between real and nominal.

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debtor countries. Without appropriate policies in the debtor countries themselves there can be no sustained progress. Another element is a favourable external environment: sustained growth in the industrial countries, expanding trade, and the avoidance of a resumption of high interest rates. A third fundamental element of the debt strategy is the availability of adequate levels of external financing.

39. There is some scope for optimism regarding all three elements of the strategy:

- many of the debtor countries are increasingly committed to the adoption of better domestic policies;
- economic activity in the industrial countries is expected to continue expanding at a moderate, but steady, pace;
- the terms of trade of the developing countries have strengthened, and although they are not expected to rise in real terms over the medium term, they should no longer be a source of weakness;
- the role of official financing is likely to grow, but the financing situation generally is expected to remain very difficult.

40. Almost all net new lending to the debtor countries is from official sources; since 1984 net private lending has shrunk considerably. Official financing has been extended on a large scale through the Paris Club: since 1983 over \$20 billion of debt-service payments by countries of the Western Hemisphere and Asia have been consolidated, of which a sizeable proportion represent rescheduled interest payments. Official financing and the international financial institutions should continue to play a central role in the debt strategy. Speedy approval and subscription by all governments to the \$74.8 billion general capital increase for the World Bank will substantially increase available resources. The IMF is providing additional financing to the poorest indebted countries through the enhanced structural adjustment facility (ESAF), and the modified extended Fund facility (EFF) will provide financing on more favourable terms and will place greater emphasis on medium-term structural adjustment. Also, the incorporation into Fund programs of external contingency mechanisms would assist countries in keeping to their adjustment programs in the face of unexpected adverse external events.



Para 40. Given the usual Congressional difficulties, we (and probably the US Administration) would like communique language committing all Summit countries to speedy approval of, and subscription to, the GCI. Need big plug for ESAF; and any reference to EFF in communique should emphasise case by case treatment and need for strong domestic reform effort in recipient countries.

NBlaOM

41. In view of the fact that about two-thirds of the outstanding debt of the heavily indebted middle-income countries is held by private creditors, their continued involvement in the debt strategy is essential. While increases in loan-loss provisions have resulted in a strengthening of the Banks' financial positions, they have also made the organization of new money packages more difficult. In this regard, the international financial institutions, especially the World Bank, can play an important catalytic role in mobilizing additional financing from private and official sources in support of countries' adjustment programs.
42. In addition to traditional rescheduling exercises, in recent years there has been increasing recourse to debt transformation and debt reduction techniques. The important characteristics of these financing techniques are that they are voluntary, market oriented, and applied on a case-by-case basis. To date, the "menu approach" has worked mainly to transform the nature of debt claims. However, the emergence of innovative approaches, such as the Mexican bond-swap scheme, could help reduce the existing stock of debt. The flexibility of the present strategy would be enhanced by the further broadening of the menu approach and the encouragement of innovative financing techniques.

Debt of the Poorest

43. Progress in dealing with the debt burden of the poorest developing countries has been encouraging:
- the recent enhancement of the IMF's Structural Adjustment Facility by SDR 6 billion will substantially increase disbursements on highly concessional terms to low-income countries;
 - the World Bank, in conjunction with ODA agencies, has put in place an enhanced program of co-financing aimed at the poorest countries;
 - Paris Club creditors are rescheduling debt at extended grace and repayment periods.
44. In cases where it is extremely difficult for countries to meet their debt-service obligations, an increase in concessional resource flows will be necessary to help those countries resume sustained growth. One proposal is to reschedule the commercial debts of the poorest countries at concessional interest rates. An alternative,

Debt of the
poor

DGB
THG
POOR



41. IFIs' 'catalytic' role OK, but resist language on Fund/Bank guarantees of new commercial bank money packages (only appropriate in exceptional circumstances).

44. First proposal is Chancellor's. Second is new Canadian/... proposal put to Paris Club. We want endorsement of a scheme at Toronto. Last sentence contains French proposals, which we regard as inadequate response (lowering of spreads etc must not be run as an alternative to the proposals earlier in this paragraph). We shall brief further before the Sherpas' meeting. The Chancellor is meeting the Canadian Finance Minister on 16 July.

- No reference to aid targetry (0.7% of GNP) as such, but the reference to 'an increase in concessional resource flows' will need watching; in the present context it is fine because it leads into the Chancellor's proposal.

NBLAOM

if less far-reaching, proposal is to allow creditors to choose between shorter repayment periods at concessional rates and longer repayment periods at commercial rates. The adoption of either proposal would be a positive development, especially if the interest relief is additional to countries' existing aid programs. Other techniques for reducing the burden of debt service should also be explored, notably in the areas of ODA debt cancellation and the lowering of interest rate spreads and fees charged by export credit agencies on rescheduled debt.

45. The debt burden of low-income countries is part of a broader developmental challenge. The developing countries themselves need to persist with efforts to implement effective programs of structural reform and macroeconomic adjustment. Developed countries need to support these programs over time with opportune and adequate concessional resources.

cc Mr Hutton
Mr Savage Holt

cc Mr Fitten ECDE
Mr Wright Economic Advisor
Mr Douce

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ORGANISATION FOR ECONOMIC
CO-OPERATION AND DEVELOPMENT

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paper CE (88)9 ii para
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see OECD
docs

COUNCIL
AT MINISTERIAL LEVEL

THE ASIAN NICs AND OTHER MAJOR DEVELOPING ECONOMIES
IN THE WORLD ECONOMY

(Note by the Secretary-General)

- I. NEW REQUIREMENTS FOR POLICY ANALYSIS AND CO-OPERATION
- II. CHANGING PATTERNS AND INVOLVEMENT IN THE WORLD ECONOMY
- III. SPECIFIC SITUATIONS AND POLICY ISSUES
- IV. BROAD ORIENTATIONS FOR THE OECD
- V. QUESTIONS FOR DISCUSSION

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I. NEW REQUIREMENTS FOR POLICY ANALYSIS AND CO-OPERATION

1. The emergence of a more global economy -- reflecting the continued rise in trade as a proportion of total world output, faster diffusion of technological progress, the globalization of financial markets and the pursuit of outward oriented policies in a number of developing countries -- is a fact. It is creating new potential for advances in human welfare to spread around the world. But important adjustments and policy issues are involved also. The capacity to cope with change and new competitive forces varies considerably within and among countries. The transmission of policy actions has become more widespread, and their effects more difficult to grasp or predict.

2. The emergence of the four Asian NICs -- Korea, Taiwan, Singapore and Hong Kong -- as significant actors in the world economy has been a particularly remarkable phenomenon over the last decade. But there are also other economies and situations where the actual or potential interactions with OECD countries pose significant challenges and opportunities.

3. The traditional country categories, developed and developing, OECD and non-OECD, in terms of which much policy analysis and discussion has hitherto been conducted, are becoming an increasingly inadequate framework for understanding the major trends and issues in the world economy. The heterogeneity of the developing countries has to be recognised and more adequately treated.

4. The Secretariat has undertaken a study to assist Members to assess the implications of this evolution for policy analysis and co-operation in the OECD framework. It would be helpful, at this stage, to discuss the broad orientations along which the OECD's role might be most effectively and appropriately exploited to meet these new requirements.

5. Clearly, political as well as substantive questions are involved in finding suitable approaches. It will be essential to

develop a better appreciation as to how the major developing economies themselves perceive their own situations in the world economy, their problems and their future evolution.

6. Against this background, special attention might be devoted to the case of the Asian NICs, given the urgent need to find ways for them to participate more effectively in discussions on policy co-operation and international adjustment.

II. CHANGING PATTERNS AND INVOLVEMENT IN THE WORLD ECONOMY

1. New Patterns of Trade: Shifting Comparative Advantage

7. The last decade or so has witnessed a major shift in the pattern of international specialisation. During the previous century and a half, until the 1960s, international specialisation was reflected in an international trade pattern where, predominantly, commodities were exchanged for manufactured goods. Trade in manufactures between developing countries and developed countries was relatively insignificant, and reflected relative endowments of capital and labour, with low cost labour providing the developing countries with comparative advantage in certain labour intensive products.

8. This traditional pattern has of course been changing for a number of years. Trade in manufactures has risen from 50 per cent of total world trade volume in 1960, to over 75 per cent in 1985. And the share of developing countries in world manufactures trade has increased from 7 per cent in 1965 to 17 per cent in 1985. But the pace of change in the pattern of trade and the character of international specialisation may be accelerating under the influence of two main factors:

- the major advances in technologies, particularly micro-electronics, with wide application in production

and communication, and the falling costs of such applications;

-- the rapid accumulation of physical and human capital in a range of developing countries

9. In combination, these factors are beginning to alter the basis for international specialisation away from resource endowments and labour costs towards the capacity for specialized production based on technology generation or absorption and the capacity to adjust production rapidly to meet changing opportunities on global markets. Comparative advantage, far from being a "given", becomes something that, with varying degrees of difficulty, can be shaped and reshaped by entrepreneurial activity, and hence assumes a more dynamic character. Intra-industry trade, product differentiation and economies of scale become more general. A market-driven enterprise culture becomes a more important national asset.

10. This phenomenon is relatively recent. The more traditional patterns of specialisation and trade continue to be the mainstay for many countries, developed and developing. Labour costs and resource endowments remain important factors in international specialization.

11. Among the developing countries, it is the Asian NICs -- Korea, Taiwan, Hong Kong and Singapore -- which have most successfully adapted to the new possibilities for international specialisation. The key factors in their success have been an appropriate set of policies to foster "outward-looking" economic development, efficient use of resources and the expansion of high-quality education at all levels. These economies are now at varying stages of a shift from labour-intensive production to knowledge-intensive activities.

12. A range of other developing countries -- a number of ASEAN countries, some Latin American countries and also China and India -- have the potential to evolve capacities similar to those of the Asian NICs in terms of human resources and the absorption and use of

technology. The full realization of this potential will depend, however, on finding solutions to various domestic structural problems that weigh on the economies of these countries.

13. This evolving pattern of specialisation in the world economy is associated with a globalization of technologies, markets and finance in which the Asian NICs are participating. New kinds of corporate strategies have appeared, including corporate alliances and corporate networking aimed at exploiting or acquiring technology and markets. Against this background, a range of domestic and international policy issues bearing on the international competitiveness of OECD countries has emerged, in such fields as education, personal and corporate taxation, financial market regulation, information and communications, research and development policies and funding, technology transfer, intellectual property, trade in services and foreign investment measures and regimes.

14. To the extent that the major developing countries become active in the new pattern of specialisation, these issue-areas become relevant to their situations. Significantly, a number of such "new" issues constitute negotiating themes in the Uruguay Round in which developing countries are participants.

2. The Macroeconomic Context

15. Major developing economies have not only been actors in the structural evolution of the world economy over the last decade or so, they have also generated or been involved in some of the principal macroeconomic interactions.

16. The large OECD current account imbalances, while reflecting mainly interactions among the major OECD countries, have also to be seen in a more global context. Import compression in major Latin American debtor countries has helped to widen the United States trade deficit. Falling oil prices have increased the German and Japanese surpluses. And the current account surpluses in Taiwan and

Korea now represent an important counterpart to the United States current deficit.

17. There is considerable complexity in the macroeconomic interactions between OECD economies and non-OECD economies. A global perspective rather than an OECD-centered perspective is necessary to bring into focus the different lines and nature of such interactions. An important case in point is the "triangular" relationship which has developed between Japan, the Asian NICs and the United States, in which the NICs have, to date, largely bought capital equipment and sophisticated components in Japan and sold the output in the United States market. The open US market has thus been central to the industrial strategies of the Asian NICs.

18. Major developing economies have represented important growth poles in the world economy. In the 1970s, Latin America, the oil producers, and the Asian NICs were all growing rapidly, representing dynamic export markets for OECD countries and generating demands for commodities that helped to raise the terms of trade for poorer developing countries. In the 1980s, only the Asian countries have continued as a growth pole. Taking China, Japan, the Asian NICs and ASEAN together, the East Asian region now represents the most dynamic market in the world economy.

III. SPECIFIC SITUATIONS AND POLICY ISSUES

19. To understand the way in which these structural and macroeconomic factors are operating to reshape the world economy it is necessary to look at specific country and regional situations. The following analysis treats first the situations of the Asian NICs and then the position of a range of other major developing economies.

1. The Asian NICs

20. A distinguishing feature of the Asian NICs has been their commitment to an export-led development path. Also in common is the

striking increase in their domestic savings rates from very low levels at the beginning of the 1960s to extraordinarily high levels today. Fiscal management has been generally prudent in all countries.

21. In other respects, however, their economic strategies have been quite different. Hong Kong has operated with virtually no government intervention in the allocation of resources; in Singapore, Korea, and Taiwan there has been a significant Government role. Singapore, Taiwan and Hong Kong have welcomed foreign investment; Korea has preferred to license technology and borrow on financial markets. Hong Kong and Taiwan have many small firms engaged in exporting; Korea has developed large conglomerates; Singapore has fostered a multinational enterprise sector. Hong Kong and Singapore have virtually free trade regimes and open financial markets. Korea and Taiwan have used protection as a part of their industrial policies (although trade is now being liberalized in both cases); and their domestic financial markets have been tightly regulated, and remain to be further developed in certain important respects. Exchange rates have been managed in all four economies but in different ways and with different objectives.

22. In terms of political status there are also important differences. All four Asian NICs have faced uncertainties, both internal and external. Hong Kong is now entering into a period of political transition, Taiwan and Korea are also experiencing political change while a new generation of political leadership is emerging in Singapore.

23. With these important differences in situation and economic policies it is hardly surprising that these economies do not see themselves as constituting a group. They are widely referred to as such by outside observers essentially because of the similar evolution of their roles in the new pattern of international specialisation described earlier. And developments in the world macroeconomy in the 1980s have had, against this background, broadly similar impacts on their export patterns and performance.

24. Essentially, in the first half of the 1980s, the United States import market emerged as the only significant growth market in the OECD economy. In volume terms, United States imports grew at nearly 5 per cent per annum, twice the rate of import growth in the rest of the OECD area. As is clear from Chart 1, the result was a dramatic increase in US imports as a share of world imports. This powerful demand "pull" was matched by the extremely flexible supply responses which are the hall-mark of the Asian NICs. While not uniformly in step, their export volumes grew vigorously in parallel with US import volumes.

25. The dynamic export growth of the Asian NICs has continued through the current phase of dollar depreciation and adjustment in the real United States trade balance. A major reason for this is that the United States adjustment is being effected largely through a massive increase in United States export volumes. This expansion is projected to more than offset the US loss of world market share in the early 1980s (See Chart I). United States import volumes have continued to grow at a substantial rate and a significant portion of this import growth is being met by the Asian NICs, partly replacing imports from Japan.

26. With the rise in the yen and the reorientation of Japanese growth towards the domestic economy, Japanese export volume is projected to remain static through the rest of the decade. At the same time Japanese imports of finished products and components from the Asian region have begun to expand significantly. This development is in part linked to growing outflows of Japanese direct investment to the Asian region.

27. The new exchange rate relationships between the dollar, the yen, and the currencies of the Asian NICs are facilitating this pattern. With growing export markets in both Japan and the United States, the export volume growth of the Asian NICs is projected to remain dynamic through to the 1990s (see Table 4). And these economies are also increasing their exports to the European countries.

28. As a counterpart to this buoyant export growth, the import volumes of the Asian NICs from the United States and, to a lesser extent, Europe, are also growing rapidly. In the case of Singapore and Hong Kong, import growth is broadly matching export growth. In the case of Taiwan and Korea, however, large current account surpluses have emerged, and these are currently projected to diminish only slowly over the next year or two.

29. The origins of the Taiwanese and Korean surpluses are different. In the case of Taiwan, the current account surplus began to emerge earlier with a significant decline, from the early 1980s, in the investment to GDP ratio, due in part to political uncertainties, but also to the underdevelopment of the financial and corporate sectors. In the case of Korea, the current account surplus has emerged more recently, as a counterpart to a steady climb in the savings ratio, associated in particular with rapid growth in personal incomes, itself related to rapid export growth. Part of this savings increase may prove to be temporary as and when growth settles down to a more normal pace. In both economies, exchange rates have been very competitive throughout the 1980s. In Korea, policy settings over this period were very much shaped by the need to achieve substantial external adjustment to deal with high levels of external debt.

30. The international policy issues surrounding the Korean and Taiwanese surpluses require however, careful consideration. Domestic policies in these economies are pointing to a resetting of national priorities and growth orientations through deregulation of financial markets and foreign exchange controls, continuing liberalisation of formal and informal trade barriers and further exchange rate appreciation. These domestic orientations have wider international implications. They lead in the direction of a further upgrading of economic structures and hence a further evolution in the role of these economies in the pattern of international specialisation. Other developing countries in the region are likely to benefit from resulting shifts in industrial location.

31. On a more macroeconomic level, the speed and degree of adjustment in these economies has to be seen in relation to the speed and nature of current account adjustment in the United States and other regions as well. With their high savings rates, these economies may emerge as structural capital exporters to some degree, even after significant adjustment has occurred.

32. Adjustment and structural evolution in the Asian NICs should create new opportunities for OECD countries in trade and investment and contribute to stable and sustained world economic growth. But OECD countries must also be prepared to accept new competitive pressures and should actively attempt to understand and assist the consequent changes in world economic patterns.

2. Other Major Developing Economies in Asia

33. In the Asian region, the other developing economies where interactions with OECD economies are significant include three countries which are major exporters of primary products, but who are rapidly increasing their exports of manufactures -- Malaysia, Thailand and Indonesia -- and the two largest countries -- China and India.

34. Of the three ASEAN countries, Malaysia and Thailand have already established significant manufacturing capabilities, including through foreign investments and their general policy orientations are by and large propitious for further advances. Indonesia is less advanced, but has made important progress in recent years in diversifying its sources of public and export revenues away from oil. These countries do not yet have the human resource nor, in consequence, the managerial and technological capacities, of the Asian NICs. Such differences provide a basis for the evolution of a growing interrelationship within the region, in which Japan, especially with the appreciation of the yen, is playing a key role through trade and investment flows. Clearly, there are important opportunities for other OECD countries also, and

many are active in the region.

35. China is increasingly to be seen as an actor in the growing international role of the Asian region. The modernization and opening up of China's economy will be of major international importance. China's exports and imports are growing rapidly -- China is already the largest single developing country market for OECD exports (See Table 2). Hong Kong is making an important contribution to these developments as a channel for trade and investment, with Hong Kong entrepreneurs taking an active role.

36. India has important human resources and technological capacities, which could be the basis for more involvement in the international economy in the future than has been the case in the past. There are indications of an awareness in India of the opportunities created by new developments in international specialisation. Major policy and structural changes are required however for India to assume an important global economic role. Some economic liberalisation has taken place, with the priority being placed on internal deregulation of the industrial sector, rather than on trade liberalisation. Higher sustainable growth and the maintenance of external financial stability are likely to need to be underpinned by an increase in export orientation.

3. Major Developing Economies in Latin America

37. The structural developments in the world economy in the 1980s have had some positive spin-off for major Latin American economies, including the growth of US-oriented investment and exports in Mexico particularly. But the debt-related plunge in their investment ratios and their inability to find effective solutions to domestic stabilisation problems has constrained their ability to take advantage of the new possibilities for international specialisation. As a result, they have been falling behind the Asian countries as participants in the globalisation of production and markets and in economic performance more generally.

38. The human resources and the industrial and technological capacities to take on an important role in the global economy exist in the major Latin American economies, especially in Brazil and Mexico. Major policy reorientations will be essential however. Economic stabilisation will be a first essential, but requires fiscal and governmental reforms which are subject to complex socio-political problems. This interdependence of structural adjustment, macroeconomic imbalances and socio-political constraints in the major Latin American economies presents a major challenge.

IV. BROAD ORIENTATIONS FOR THE OECD

39. The foregoing highlights the growing need for the Organisation to know better the circumstances, policies, and aspirations of a range of major developing economies and to explore avenues for consultations between these and OECD countries in order to further improve the functioning of the world economy. The most pressing need is to apply this approach to the Asian NICs.

40. The main areas where there could be mutual interest in policy discussions and co-operation with the Asian NICs are the following:

- a) macro-economic management, including exchange rate policies and current account imbalances;
- b) liberalisation of trade, investment flows and domestic capital market;
- c) structural adjustment issues in the light of increased international competition and technological change;
- d) specific sectors or policy areas where strengthened contacts could be useful.

41. The OECD has certain comparative advantages which could make it an appropriate forum to take up such policy issues. It is a

multi-disciplinary organisation, with a broad agenda and flexible procedures, limited operational responsibilities, and is based on the deliberations of Committees that bring together the responsible government officials working in Capitals. It has established procedures for carrying out policy and country reviews using peer group techniques. Given the diversity of the issues and countries a "variable geometry" approach might be adopted, with modalities which would vary according to the issues and countries involved.

42. The following lines of approach could be used, as appropriate.

i) Policy-oriented country and/or issue studies

Policy-oriented country and/or issue studies could be undertaken to deepen OECD countries' understanding and to better relate the issues arising from specific situations to the broader international context. The emphasis of such studies could be on linkages with OECD policies and on options for co-operation with Asian NICs. It would be desirable that such work be undertaken in co-operation with the non-Member economies concerned.

ii) "Rules of the Game" discussions and OECD Codes

The OECD establishes and maintains certain multilateral disciplines in the form of Codes, or other inter-governmental agreements (e.g. OECD Liberalisation Codes, OECD Declaration on International Investment and Multinational Enterprises, the National Treatment Instrument). In some cases, certain Asian NICs might in the future be invited to participate, first in the exchange of relevant policy information and experiences on an informal basis, and then eventually, in an appropriate form which would not necessarily imply adherence to OECD, in the Codes or other agreements on the basis of equal rights and obligations.

iii) Liaison Committees or Committee Observerships

It might be possible to extend to some non-Members ties with certain Committees in a way acceptable to both sides. These modalities could be envisaged not only at the level of any relevant Committee (or sub-group), but also in cases where a cross-sectoral dialogue is found to be desirable.

iv) Informal contacts

In addition to the approaches mentioned above and in order to prepare for them, it is also possible to think of a variety of informal and exploratory contacts.

43. In moving in such directions, it would be important of course to avoid duplication of work done by other international organisations and, where possible, to draw on information, analyses and consultations within these organisations.

44. The broad approach outlined above for developing the Organisation's work and co-operation with the Asian NICs could be applied also to other major developing economies, with appropriate variations in the substantive focus. Applying the approach to the Asian NICs should be the first priority however. It would be essential to proceed with caution, pragmatism and flexibility, given the specificity of each of the Asian NICs, and the uncertainty in predicting their reactions.

45. In the light of the reaction to these broad orientations for OECD work as well as the considerations that will emerge from the Working Party on these issues which was established by the Council on 4th May, 1988, the Secretary-General could submit, at a later stage, more detailed proposals. The question of the resources necessary for such additional work will, of course, have to be borne in mind.

V. QUESTIONS FOR DISCUSSION

Taking account of the foregoing, it is suggested that discussion be based on the following questions:

- i) Are these broad orientations for OECD work on relations with major developing economies, and the Asian NICs in particular, generally acceptable?
- ii) How might contacts and consultations with Asian NICs best be handled?

Table 1
SUMMARY INDICATORS FOR MAJOR DEVELOPING ECONOMIES AND THE OECD

	World GNP share (Per cent) (a)		GNP per capita (US \$)	Real GNP/GDP growth (per cent)			Trade orientation: Exports as % of GDP (b)			Savings and investment ratios (b)					
	1965	1985		1985	1965-73	1973-80	1980-86	1965	1980	1985	Savings/GDP (%)			Investment/GDP (%)	
			1960								1980	1985	1960	1980	1985
Asian NICs	0.6	1.8	2 946	10.0	7.9	7.6	--	--	--	--	--	--	--	--	--
Hong Kong	0.1	0.3	6 230	7.9	9.0	6.3	71	111	106	6	24	28	18	29	21
Korea	0.2	0.8	2 150	10.0	7.3	8.4	9	37	36	1	23	31	11	31	30
Singapore	0.1	0.2	7 420	12.5	7.5	6.6	123	--	85	-3	30	42	11	43	43
Taiwan	0.2	0.5	3 120	11.0	8.1	7.4	19	53	56	13	33	32	17	31	19
Latin American MDEs	3.7	4.0	1 842	7.7	5.9	1.0	--	--	--	--	--	--	--	--	--
Argentina	1.3	0.6	2 130	3.8	2.2	-1.5	8	--	15	21	--	16	22	--	9
Brazil	1.2	1.9	1 640	9.4	6.8	1.9	8	9	14	21	20	22	22	22	16
Mexico	1.1	1.5	2 080	7.6	6.1	3.3	9	14	16	18	26	26	20	28	21
Big Asian Two	(6.6)	4.2	293	5.8	4.8	8.0	--	--	--	--	--	--	--	--	--
China	(3.7)	2.4	310	7.5	5.2	9.4	4	6	11	23	30	34	23	31	38
India	2.9	1.8	270	3.6	4.0	5.3	4	7	6	14	20	21	17	23	25
ASEAN Three	0.6	1.3	691	7.6	7.0	4.4	--	--	--	--	--	--	--	--	--
Indonesia	0.2	0.7	530	7.6	6.9	4.3	5	31	23	8	30	32	8	22	30
Malaysia	0.2	0.3	2 000	7.1	7.5	3.7	42	60	55	27	32	33	14	29	28
Thailand	0.2	0.3	800	8.0	6.8	5.0	18	25	27	14	22	21	16	27	26
OECD (c)	79.6	78.2	11 810	4.7	2.6	2.4	12	20	18	22	22	21	21	23	21
Selected OECD economies															
Group of Seven economies															
United States	39.7	35.9	16 690	3.7	2.2	2.6	5	10	7	19	17	16	18	18	19
Japan	5.2	11.9	11 300	9.8	3.8	3.7	11	14	15	34	31	32	34	32	28
Germany	6.5	5.6	10 940	4.3	2.4	1.4	18	28	33	29	25	24	27	25	20
Smaller OECD economies															
Greece	0.3	0.3	3 550	7.5	3.4	1.3	9	19	22	11	20	9	19	28	21
Portugal	0.2	0.2	1 970	7.2	2.7	1.5	27	28	39	12	11	20	19	25	21
Spain	1.3	1.5	4 290	6.5	2.3	1.7	11	16	23	22	18	22	19	21	19
Sweden	1.2	0.9	11 890	3.4	1.7	1.7	22	30	35	24	19	21	25	21	19
Switzerland	0.8	0.9	16 370	4.1	0.4	1.6	29	37	39	29	23	25	29	27	24
Turkey	0.5	0.5	1 080	6.5	4.3	5.1	6	7	19	13	18	16	16	27	20

- a. Based on data excluding the European CMEA economies, Albania, North Korea and Mongolia.
 b. Where data for the years cited are unavailable, figures for a year either side of that year are quoted.
 c. The figures on per capita GNP, trade orientation and savings and investment ratios are based on statistics which exclude Greece, Iceland, Luxembourg, Portugal and Turkey.

Source: World Tables 1987 (draft), World Bank and International Finance Corporation; World Development Report 1987, World Bank; and the World Bank and OECD data bases.

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Table 2
MDEs' AND TRADE

	Exports 1986	of which: to OECD	Imports 1986	of which: from OECD	Exports Growth 1966-80	Exports Growth 1980-86	Imports Growth 1966-80	Imports Growth 1980-86
	\$ billion (a)				Per cent, per annum (b)			
<u>Asian NICs</u>	130.1	85.8	111.5	64.3
Hong Kong	35.4	18.0	35.6	15.3	11.0	8.6	9.0	7.9
Korea	33.9	25.5	29.7	21.1	25.0	11.4	14.7	9.4
Singapore	21.2	9.1	23.6	11.4	5.9	5.8	7.9	4.4
Taiwan	39.5	33.2	22.6	16.5	19.5	12.7	15.5	2.9
<u>ASEAN Three</u>	36.2	27.9	30.3	16.0	7.3	5.5	6.6	-0.8
Indonesia	13.8	12.9	11.6	6.1	9.1	1.0	15.5	-1.8
Malaysia	13.7	9.2	10.3	5.2	4.9	9.2	4.3	-0.8
Thailand	8.7	5.8	8.4	4.7	8.0	10.5	3.2	0.9
<u>Big Asian Two</u>	36.3	22.6	51.2	32.4	4.8	8.1	5.0	10.7
China	25.8	16.0	34.9	22.2	5.5	9.7	7.7	14.7
India	10.5	6.6	16.3	10.2	3.5	4.2	2.4	3.9
<u>Latin American Three</u>	45.4	43.2	30.5	27.8	8.3	4.4	7.0	-6.7
Argentina	7.0	4.0	4.9	3.1	4.1	2.4	4.4	-11.1
Brazil	22.4	17.5	14.2	9.4	9.7	3.2	7.1	-4.0
Mexico	16.0	21.7	11.4	15.3	9.9	6.7	8.6	-8.5

- a. Merchandise exports/imports in current US dollars.
b. Merchandise exports/imports at constant 1980 US dollar prices.

Source: World Tables 1987 (draft), World Bank and International Finance Corporation; and OECD data base.

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Table 3

ASIAN NICs AND INTERNATIONAL ADJUSTMENT IN 1986-7
\$ US billion

	Merchandise Trade Balance								Current Account		External debt (a)		Foreign Reserves	
	Total		with USA		with Japan		with OECD Europe		1986	1987*	1986	1987*	1986	1987*
	1986	1987*	1986	1987*	1986	1987*	1986	1987*	1986	1987*	1986	1987*	1986	1987*
Taiwan	16.9	22.1	14.6	17.4	-3.2	-4.3	2.7	4.0	16.2	21.1	4.4	..	46.3	75.5
Korea	4.1	7.8	7.0	9.4	-5.2	-5.2	1.8	3.4	4.6	10.2	46.8	30.2	8.6	11.1
Hong Kong (b)	-0.1	-0.2	5.8	5.9	-6.1	-7.4	1.6	2.0	1.6*	1.2
Singapore	-2.3	-3.0	1.3	2.1	-3.1	-4.0	-1.1	-1.2	0.5	-0.1	2.0	1.5	12.9	13.5

* Estimates.

a. Public and publicly-guaranteed.

b. The current account estimates for Hong Kong correspond to the balance between exports and imports of goods and services on a National Accounts basis; investment income and transfers are excluded from this definition.

Source: IMF and OECD data bases and the US Department of Commerce.

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Table 4

TRADE AND CURRENT BALANCES OF ASIAN NICs

Current Balances

(\$ billion)

	1986	1987 (est.)	1988	1989
Korea	4.6	9.8	8	7 1/2
Taiwan	16.2	20.0	20	17
Hong Kong (a)	1.5	1.8	2	2
Singapore	0.5	0.2	- 1/2	- 1/2
TOTAL	22.9	31.8	30	26

Trade volumes

(Percentage changes)

	<u>Export volumes</u>				<u>Import volumes</u>			
	1986	1987 (est.)	1988	1989	1986	1987 (est.)	1988	1988
Korea	13.3	26	19	17	8.4	23	27	20
Taiwan	25.0	19	16	16	29.3	30	35	27
Hong Kong	14.6	30	26	18	13.0	30	25	20
Singapore	13.4	14	13	14	8.9	10	14	14
TOTAL	17.2	23	19	16	14.2	24	25	20

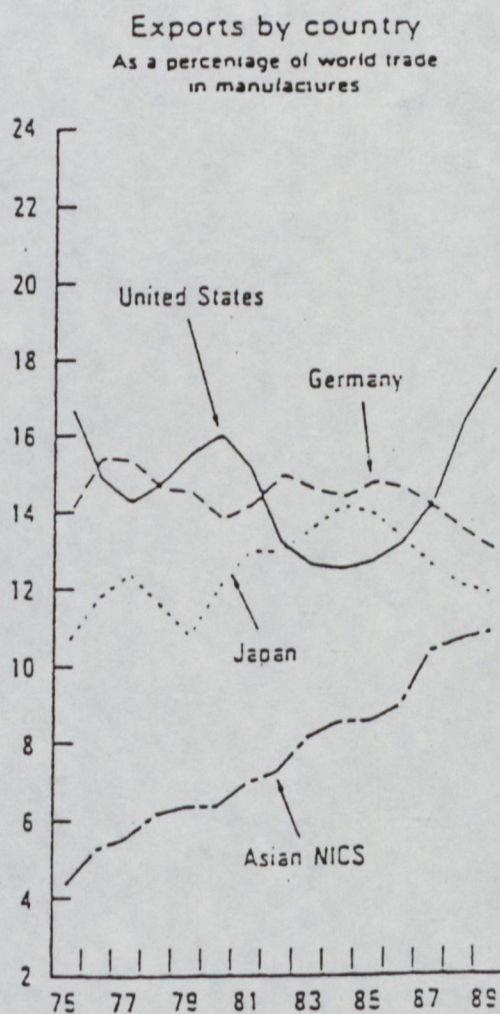
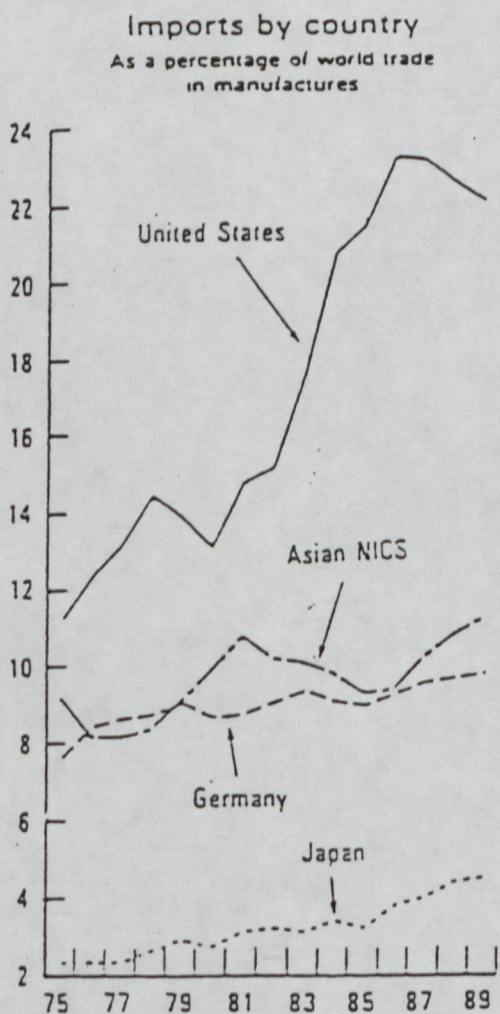
Memorandum item:

% of world trade								
Asian NICs	6.6	7.4	8.3	9.4	5.7	6.5	7.7	9.0
Japan	10.4	9.7	9.8	9.5	5.8	5.7	6.2	6.2
Germany	12.1	12.4	11.9	11.4	8.9	9.2	9.2	9.1
USA	11.1	10.9	12.1	13.2	18.8	18.1	17.4	17.1

- a. Estimates for Hong Kong correspond to the balance between exports and imports of goods and services on a National Accounts basis; investment income and transfers are excluded from this definition.

Sources: IMF, International Financial Statistics; The Central Bank of China, Financial Statistics: Taiwan District, The Republic of China; Hong Kong Census and Statistics Department, Monthly Digest of Statistics.

Chart I
Shares of World Trade in Manufactures



Source: OECD Economic Outlook No.42, December 1987.

MFF 090 / NIK

(p. 11-19)

Mr. V. J. ...
Mr. Feetman, (HIC)
Mr. Dennis, (S...)
Mr. Fitter, (EC) (E).
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OECD EXECUTIVE COMMITTEE IN SPECIAL SESSION: 2-3 MAY

SUMMARY

1. A GUARDED DISCUSSION ON TRADE AND AGRICULTURE, WITH NO MAJOR PLAYERS PREPARED TO SHOW THEIR HAND BEFORE THE OECD MINISTERIAL. US AND CANADA SUBJECTED OVER DINNER TO ARGUMENTS AGAINST RAISING THE TEMPERATURE AT OECD OR TORONTO. BUT US INTENTIONS REMAIN UNCLEAR.

2. A GOOD EXCHANGE ON RELATIONS WITH THE NICS. AGREEMENT ON NEED FOR DIALOGUE. MAJORITY FAVOUR INFORMAL CONTACTS, POSSIBLY A SEMINAR AS FIRST STEP. NO FIRM VIEW ON WHICH NICS TO INCLUDE, BUT ASIANS GENERALLY PREFERRED TO LATINS. PAYE TO INTRODUCE SUBJECT AT OECD MINISTERIAL WORKING LUNCH.

DETAIL

ECONOMIC SITUATION

3. HENDERSON (OECD SECRETARIAT) GAVE AN ASSESSMENT OF WORLD ECONOMIC PROSPECTS IN LINE WITH LAST WEEK'S ECONOMIC POLITICAL COMMITTEE. GROWTH WAS STRONGER THAN EXPECTED BUT IMBALANCES WERE SHRINKING MORE SLOWLY. NO-ONE CHALLENGED HIS ANALYSIS.

TRADE AND AGRICULTURE

4. THE SECRETARY-GENERAL'S LATEST REDRAFT OF THE OECD MINISTERIAL COMMUNIQUE APPEARED SHORTLY BEFORE THE MEETING, TOO SOON FOR MOST DELEGATIONS TO REACT.

5. KRENZLER (EC COMMISSION) WARNED AGAINST BECOMING MESMERIZED BY THE URUGUAY ROUND MID-TERM MEETING (MTM), TO THE DETRIMENT OF PROGRESS IN GENEVA. IT WAS TOO

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EARLY TO IDENTIFY SPECIFIC OBJECTIVES FOR MONTREAL. THE COMMISSION WOULD OF COURSE LIKE TO SEE PROGRESS ON SERVICES, TRIPS, DISPUTE SETTLEMENT AND FOGS, BUT NOT AT THE EXPENSE OF GLOBALITY. THERE WERE DANGERS OF AROUSING UNREALISTIC EXPECTATIONS OF THE MTM, WHICH SHOULD NOT BE TURNED INTO A MEDIA EVENT. THE COURAGEOUS STEPS TOWARDS AGRICULTURAL REFORM AGREED AT FEBRUARY'S EUROPEAN COUNCIL MUST BE FOLLOWED AND NOT UNDERMINED BY OTHERS.

6. ABERG (SWEDEN) AND SCHOMERUS (FRG CHAIRMAN OF OECD TRADE COMMITTEE) WERE NOT UNDULY ALARMED BY THE CURRENT SLOWDOWN IN GENEVA: MAJOR CONCESSIONS SHOULD NOT BE EXPECTED AT THIS STAGE OF THE MTNS. OTHER EC MEMBER STATES (EXCEPT IRELAND) REMAINED SILENT.

7. WALLIS (US) WANTED THE MTM TO PRODUCE CLEAR COMMITMENTS AND TANGIBLE RESULTS. THE MOST PROMISING AREAS WERE SERVICES, AGRICULTURE, TRIPS, TRIMS AND INSTITUTIONAL REFORMS. THE OECD MINISTERIAL COMMUNIQUE NEEDED FURTHER AMENDMENT TO REFLECT THIS OBJECTIVE. MEMBER STATES HAD NOT BEGUN TO REFORM THEIR AGRICULTURAL SUPPORT PROGRAMMES. THE MTM SHOULD AIM TO SET IN PLACE A FRAMEWORK FOR LONG TERM MARKET-ORIENTED REFORM.

8. MRS OSTRY (CANADA) THOUGHT MACROECONOMIC CONSTRAINTS MADE THE URUGUAY ROUND ALL THE MORE IMPORTANT. TO GIVE A CREDIBLE SIGNAL, THE MTM MUST ADOPT A PACKAGE OF MEASURES INCLUDING AGRICULTURE. BLANKART (SWITZERLAND) AND FORTUNE (NZ) WERE WORRIED THAT THE URUGUAY ROUND WAS NOW IN TROUBLE. FORTUNE, BACKED BY VISBORD (AUSTRALIA), CALLED ON THE EC, US AND JAPAN, TO TRY HARDER ON AGRICULTURE. THE CAIRNS GROUP PROPOSALS WERE HELD AS A SENSIBLE COMPROMISE BETWEEN THE EC AND US EXTREMES.

9. AT THE BUREAU DINNER, OSTRY TOOK THE VIEW THAT OECD MINISTERS AND THEN THE TORONTO SUMMIT MUST GIVE A STRONG AND DETAILED PUSH TO AGREEMENTS FOR THE GATT MTM. BRAITHWAITE (UK, CHAIRMAN) AND KRENZLER ARGUED THAT THIS WAS PREMATURE, AS THE INTENSE NEGOTIATING PHASE FOR THE MTM HAD YET TO START. A LOW KEY RESULT FROM OECD AND TORONTO WOULD DO NO HARM: A PUBLIC ROW AT EITHER WOULD BE DAMAGING. WALLIS SAID LITTLE.

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10. THE AMERICANS DID NOT SEEK TO REOPEN THE DEBATE ON INVESTMENT FOLLOWING THE AGREEMENT REACHED AT LAST WEEK'S OECD'S COMMITTEE ON INVESTMENT AND MULTINATIONAL ENTERPRISES.

RELATIONS WITH THE NICS

11. OYAKE (SECRETARIAT) AND PAYE INTRODUCED THE OECD PAPER, PICKING OUT THE MAJOR ISSUES. IF A DIALOGUE WERE AGREED, WITH WHOM, WHERE AND WHAT ABOUT? OF THE FOUR ASIAN DRAGONS, POLITICAL PROBLEMS IMPINGED ON TAIWAN AND HONG KONG. G7 HAD ALREADY POINTED TO THE NICS' RESPONSIBILITIES IN THE MACRO AREA: A BROADER APPROACH, INVOLVING THE NICS' OWN PREOCCUPATIONS NOW SEEMED DESIRABLE. THERE WERE ALSO INSTITUTIONAL QUESTIONS, INCLUDING FUTURE MEMBERSHIP.

12. ALL WHO SPOKE SUPPORTED THE NEED FOR DIALOGUE, GENERALLY AGREEING WITH THE SECRETARIAT APPROACH. OECD WAS NOT A CLOSED CLUB AND MUST BE OPEN TO CONTACTS WITH NEW PLAYERS. ALL SUPPORTED ESTABLISHMENT OF PROPOSED COUNCIL WORKING PARTY TO TAKE MATTERS FORWARD.

13. JAPAN (KITAMURA) SAID THE FOUR DRAGONS FELT VULNERABLE AND NEEDED CAREFUL HANDLING. JAPAN COULD HOST A SEMINAR FOR POLICY MAKERS AND PRIVATE SECTOR REPRESENTATIVES SELECTED FROM BOTH SIDES, VERY INFORMAL, PERHAPS IN A PRIVATE RESEARCH INSTITUTE UNDER OECD AUSPICES. OTHER CHANNELS SHOULD ALSO STAY OPEN.

14. US (WALLIS) LIKED THE SEMINAR PROPOSAL. OECD WAS NOT A CLOSED SHOP, BUT WAS BASED ON SHARED ASSUMPTIONS. TO TAKE IN THE NICS WOULD POSE POLITICAL AND ECONOMIC CHALLENGES. CONTACTS WERE FINE BUT NO HOPES OF EARLY MEMBERSHIP SHOULD BE KINDLED. THE NICS MUST START TAKING THEIR SHARE OF RESPONSIBILITIES. (OVER DINNER HE SAID HE DID NOT FAVOUR A PACIFIC OECD, NOR WERE MOST NICS ELIGIBLE FOR OECD MEMBERSHIP. BUT IT WAS IMPORTANT TO FIND WAYS OF TALKING TO THEM. HE TOOK A DELIBERATELY Milder LINE THAN SECRETARY BAKER).

15. CANADA (MRS OSTRY) SAID THAT OECD'S MAJOR PREOCCUPATION WAS UNWINDING GLOBAL IMBALANCES. THE ASIAN NICS' EXPORTS WOULD MATCH JAPAN'S WITHIN TEN YEARS WHILE

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THEIR DOMESTIC DEMAND WOULD BE ONLY 15% OF JAPAN'S. SHE CONTRASTED ASIAN ECONOMIES - NICS AND ASEAN COUNTRIES - WITH THE LATIN AMERICANS, WHOSE ECONOMIES WERE INWARD-LOOKING.

✓ 16. FOR THE UK, I SUGGESTED THEMES - ECONOMIC POLICY, TRADE LIBERALISATION, INVESTMENT, TECHNOLOGY TRANSFER, SERVICES AND CAPITAL MARKETS - TO FORM THE BASIS FOR A DIALOGUE. I WARNED ABOUT THE DIFFICULTIES OF INTER-GOVERNMENTAL CONTACT WITH TAIWAN, AND CAUTIONED ABOUT HONG KONG'S SENSITIVE POSITION. I EMPHASISED OECD'S WORLDWIDE CHARACTER AND THE NEED TO AVOID MAKING ANY DIALOGUE REREGIONAL IN NATURE. (SEVERAL OTHER EUROPEANS TOOK THE SAME LINE ON TAIWAN.)

17. BRAITHWAITE SUMMED UP ON THESE LINES:-

(A) THE NEED TO OPEN CONTACT WITH SOME OF THE MAJOR DEVELOPING ECONOMIES WAS GENERALLY AGREED, THOUGH WITH WHOM EXACTLY (FOUR ASIAN NICS ALONE, OR OTHERS EG ASEAN OR LATIN AMERICANS AS WELL) REMAINED UNSETTLED.

(B) THE 'VARIABLE GEOMETRY' APPROACH IN THE SECRETARIAT'S PAPER (PARAS 41-42) HAD DRAWN GENERAL SUPPORT, WITH RECOGNITION OF THE POLITICAL PROBLEMS POSED BY CERTAIN NICS.

✓ (C) THE DIALOGUE MUST BE NON-CONFRONTATIONAL AND ADDRESS ISSUES OF MUTUAL INTEREST. IT SHOULD INCLUDE TRADE AS WELL AS MACRO-ECONOMIC MATTERS.

(D) SHOULD THE DIALOGUE BE WITH A GROUP OF COUNTRIES OR INDIVIDUALS? MIGHT IT LEAD TO FUTURE MEMBERSHIP? THE NICS SEEMED NOT QUITE READY YET TO BE TAKEN IN AS EQUAL PARTNERS.

(E) THERE WAS GENERAL BACKING FOR JAPAN'S PROPOSAL FOR A SEMINAR.

(F) THE WORKING PARTY OF THE COUNCIL TO BE SET UP WOULD ADDRESS OUTSTANDING QUESTIONS AND REPORT TO THE NEXT ECSS. THE MINISTERS' LUNCHTIME DISCUSSION ON 19 MAY WOULD GIVE GUIDELINES.

✓ 18. PAYE SAID THAT HE WOULD INTRODUCE THE SUBJECT TO THE MINISTERS AT LUNCH. EVERYBODY NOW RECOGNISED IT AS AN IMPORTANT ISSUE. BUT HE SAW A RISK OF OVERLOADING THE PROCESS. HE FELT STRONGLY THAT TAIWAN SHOULD NOT BE LEFT ASIDE, BUT DID NOT WANT TO INTRODUCE NOW COUNTRIES FROM OTHER PARTS OF THE WORLD. THE LIST OF THEMES PUT FORWARD BY THE UK WAS ABOUT RIGHT. BUT THERE WAS A DANGER OF FRIGHTENING OFF THE NICS IF THE INITIAL APPROACH WAS TOO

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DETAILED. HE WAS ALSO CONCERNED THAT THE NICS, WHETHER AS A GROUP OR SINGLY, WOULD BE UNHAPPY IF FACED WITH 24 OECD MEMBERS ACROSS THE TABLE. HE LIKED THE JAPANESE IDEA OF A SEMINAR. IT SHOULD BE EXTREMELY INFORMAL. BUT IT SHOULD ALSO MAKE CLEAR THAT THE OECD WAS FIRMLY INVOLVED IN IT.

19. IN THE MARGINS OF LUNCH HEDEGARD (DENMARK) TOLD ME THAT CONTACTS WITH THE NICS MIGHT BE RAISED OVER LUNCH AT THE ARTICLE 113 COMMITTEE ON 6 MAY, WITH PARTICULAR REFERENCE TO TAIWAN.

20. NEXT ECSS MEETING 10 NOVEMBER.

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UKDEL OECD TELNO 12: RELATIONS WITH THE NICS

SUMMARY

1. THE OECD SECRETARY GENERAL WILL RAISE OVER LUNCH ON 19 MAY THE PROPOSED DIALOGUE WITH THE NICS. THE COMMISSION ASK THAT FULL MEMBERS DISCUSSION BE REFLECTED IN BRIEFING EC MINISTERS FOR THE OECD MINISTERIAL.

DETAIL

2. OVER LUNCH SCHOMERUS (PRESIDENCY) RECALLED THE RECENT ECSS DISCUSSION RECORDED IN TUR. THE PRINCIPLE OF A DISCUSSION WITH THE NICS ON MACRO-ECONOMIC ISSUES AND TRADE WAS ACCEPTED, AND HE THOUGHT THAT THE PRIORITY SHOULD BE THE ASIAN NICS. BUT THE EC NEEDED A COMMON POSITION ON HOW AND WITH WHOM TALKS SHOULD BE HELD. ROBERTS (UK) ARGUED THAT THE FIRST PRIORITY SHOULD BE THE FOUR DIAGONS, AT LEAST PARTLY ON AN INDIVIDUAL BASIS AS THE PROBLEMS WERE DIFFERENT IN EACH CASE. BUT IT SHOULD BE A TWO-WAY EXCHANGE, NOT AN INQUISITION, AND THE JAPANESE SUGGESTION OF A SEMINAR, PERHAPS UNDER PRIVATE SECTOR AUSPICES, WOULD MAKE IT EASIER TO INVOLVE TAIWAN.

3. LANDAU (FRANCE) ASKED WHETHER THE INVOLVEMENT OF THE OECD AS AN INSTITUTION MIGHT LOOK CONFRONTATIONAL. PERHAPS THE ORGANISATION OF THE DIALOGUE SHOULD BE LEFT TO THE SECRETARY-GENERAL PERSONALLY, OR SOME OTHER PROMINENT INDIVIDUAL? THE JAPANESE SHOULD NOT BE ALLOWED TO GET AWAY WITH POSING AS CHAMPION OF THE NICS. HEDEGAARD (DENMARK), AS A FORMER AMBASSADOR IN BEIJING, WAS WORRIED ABOUT CHINESE REACTION, AND THOUGHT THAT SOME ADVANCE EXPLANATION SHOULD BE GIVEN. OTHER SAW DANGERS IN APPEARING TO ASK CHINESE PERMISSION, AND KRENZLER (COMMISSION) SAW NO NEED TO TELL THE CHINESE IF TAIWAN WAS TO BE BROUGHT IN UNDER SOME NON-GOVERNMENTAL UMBRELLA. PEREZ (SPAIN) TO GENERAL AGREEMENT, SAID THAT THE DIALOGUE SHOULD BE PRESENTED AS ADDRESSING THE NICS IN GENERAL, AND NOT JUST

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THE PROBLEMS TO WHICH THE NICS GAVE RISE. EVEN IF THE FOUR DIAGONS WERE THE PRIORITY, OTHER NICS, INCLUDING THOSE IN LATIN AMERICA, SHOULD ALSO BE INVOLVED.

4. SCHOMERUS, SUMMING UP, SAID THAT THE OECD WAS THE INSTITUTION BEST PLACED TO LAUNCH THIS DIALOGUE, WHETHER OR NOT THE APPROACH WAS SEEN AS COMING FROM THE OECD AS A WHOLE OR THE SECRETARY-GENERAL. THE DIALOGUE SHOULD BE WIDE-RANGING AND NON-CONFRONTATIONAL, BUT IT WOULD AT THE SAME TIME BE AN IMPORTANT ELEMENT IN THE GATT ROUND OBJECTIVE OF INTEGRATION. TAIWAN SHOULD NOT BE LEFT OUT, BUT THE POLITICAL DIFFICULTY WITH CHINA OUGHT TO BE LESS IF ANY CONTACT WERE AS FAR AS POSSIBLE IN AN INFORMAL AND NON-OFFICIAL ENVIRONMENT. THESE POINTS COULD BE USEFULLY BE REFLECTED IN THE BRIEFING OF EC MINISTERS FOR THE OECD DISCUSSION.

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TORONTO ECONOMIC SUMMIT: THIRD MEETING OF PERSONAL REPRESENTATIVES,
19-21 MAY 1988

BRIEF NO 10: POLITICAL ISSUES

Objectives

1. To secure agreement that Heads' political agenda should include East-West, Middle East and terrorism.
2. To resist discussion by Heads of South Africa (and make clear if necessary that it would not be in the Canadian interest to raise it).
3. On terrorism, to flag the importance we attach to a robust but constructive Summit outcome.
4. To raise no objection if others strongly propose secondary topics (eg Asia), providing this does not encourage the Canadians to promote discussion of South Africa.
5. To maintain preference for a single political declaration.

Points to make

Agenda

1. Agreed that Summit leaders will concentrate on East-West. Two other key issues: Middle East and terrorism.
2. On East-West, can cover: Soviet internal - limits and extent of glasnost; difficulty of achieving perestroika; and Soviet acceptance of failure of Communism. Also Soviet external: changes of substance, as well as better PR: withdrawal from Afghanistan a major landmark, and potential for progress in Angola, but Soviet Union still determined to remain global superpower. Less change in Soviet policy towards Western Europe/NATO. President Reagan will have impressions after his visit to Moscow.
3. Should also include Eastern Europe: On the bubble; potential for trouble which could affect Gorbachev and East-West relations. Useful to share perspectives. Possible message: economic reform essential; but needs popular consent, which in turn requires political reform.
4. On Arab-Israel, leaders could support need for negotiated settlement (and US efforts), referring to international conference proposal. On Iran-Iraq could express support for those upholding freedom of navigation; call for end to hostilities and compliance with UNSCR 598; and condemn use of chemical weapons.
5. On terrorism, Kuwaiti hijacking has heightened weaknesses in



international defences. Need to regain initiative: public opinion/media will expect Summit to say something. But need to stress Summit Seven unity, not divisions.

6. UK working up ideas for constructive outcome based on five-point plan - preventive not punitive measures, not invoking Bonn Declaration. Our ideas to be discussed at special meeting of terrorism experts group, probably early June.

7. [If Canadians say Mulroney will raise South Africa if non - East-West subjects introduced]

Do not see how Summit leaders can avoid Middle East and terrorism. Do not regard Middle East (in view of dangers, volatility and superpower activity) as regional issue on a par with, for example, Philippines, Korea. In any case do not support discussion of South Africa by Heads: would be counter-productive, possibly divisive, cf Venice, Vancouver. Simply no need for discussion at this level at present.

8. [If raised by Japan] Do not wish to overburden political agenda. But no objection to brief discussion by Heads of Philippines and Korea (support democratic process) and Cambodia (under East-West) if others feel strongly. But see no focus (or need) for discussion on China.

9. [If raised by Italy]
Famine/civil war in Ethiopia best discussed by Foreign Ministers.

10. [If raised by Germany]
See no need for discussion by Heads of Central America.

Timing

11. Agree discussion of political issues over dinner on first evening. But Prime Minister may wish to raise terrorism during informal discussion on second day.

Declaration

12. UK still favours single political declaration covering East-West, terrorism and probably Middle East. Chairman's concluding press statement could cover issues discussed by Foreign Ministers.

References

A -Foreign Secretary's five point action plan on terrorism following Kuwaiti hijacking, Luxembourg 25 April.

B -Bonn Declaration, 1978.

Background

1. At the second Sherpas' meeting there was agreement that the East-West relations and the Middle East would dominate Heads' discussion, and that Sherpas would discuss any other ideas for the political agenda at their May meeting.
2. In April the Canadians trawled partners for preliminary views on the political agenda. There was consensus that East-West, Middle East and terrorism would come up; and various suggestions from others for secondary regional topics: Japan - Philippines, Korea, China, Cambodia; Italy - Horn of Africa; FRG - Central America. Partners continue to favour a single political declaration based on what leaders actually said.
3. The Canadians have reacted by suggesting that Heads cover East-West only. If regional issues are tackled, Mr Mulroney has given notice that he will raise South Africa. We have indicated that we do not think the Middle East and terrorism can be ignored, and that we continue to oppose discussion of South Africa at leaders' level.
4. East-West could cover internal political and economic developments in the Soviet Union; Soviet external policy, particularly the potential for progress elsewhere (eg Angola, Cambodia) in the light of withdrawal from Afghanistan; and arms control. The Prime Minister would also like to discuss Eastern Europe (without a suggestion that the UK should lead or urge a particular operational outcome). Policies of the Seven diverge considerably on financial relations with Eastern European countries: US makes agreement on IMF programme for Poland conditional on human rights improvements; but Japanese have pumped money into, eg, Hungary; and Italians provide credits with minimal strings.

Terrorism

5. The Foreign Secretary's five point plan (Ref A) following the Kuwaiti hijacking was put to to EC colleagues on 25 April. Preliminary ICAO reactions unenthusiastic. We are now seeking Summit Seven and EC endorsement in order to facilitate wider multilateral acceptance.
6. Canadians have been slow to respond to our proposal for an early meeting of Summit 7 terrorism experts. Meeting not now possible until early June (just before final Sherpas'/Political Directors' meeting).

7. There is no prospect of Summit Seven partners agreeing to apply Bonn Declaration sanctions (Ref B) to any of the countries involved in the Kuwaiti hijacking, although opinion could harden against Iran if incontrovertible and publicisable evidence of Iranian collusion became available. Divisive for Seven if we were to try, and fail. Thus the emphasis on preemptive, not punitive measures.

Policy Planning Staff
12 May 1988

DECLARATION ON HIJACKING MADE AT ECONOMIC SUMMIT IN BONN:

16/17 JULY 1978

The Heads of State and Government, concerned about terrorism and the taking of hostages, declare that their Governments will intensify their joint efforts to combat international terrorism.

To this end, in cases where a country refuses the extradition or prosecution of those who have hijacked an aircraft and/or does not return such aircraft, the Heads of State and Government are jointly resolved that their Governments shall take immediate action to cease all flights to that country.

At the same time, their Governments will initiate action to halt all incoming flights from that country or from any country by the airlines of the country concerned.

They urge other governments to join them in this commitment.



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MR WICKS

13 May 1988

1988 ECONOMIC SUMMIT: SHERPA MEETING ON 19-21 MAY: PARIS

Thank you for your note of ~~3~~ ^{FILE WITH NLW} May enclosing a copy of Mr Sezaki's letter of 29 April.

2. As I mentioned in my minute of 25 April, the Department of Education and Science lead on the UK's response to the Japanese Human Frontier Science Programme (HFSP), and I am grateful to them for the attached full briefing note. I endorse the general line they set out. There are no issues arising from the programme which Summit leaders should need to consider, although we should be prepared for the Japanese Prime Minister to present a brief progress report.

3. A further issue which may come up at your meeting is the International Conference on Bioethics which took place in Rome on 10-15 April. The first such conference was launched by Prime Minister Nakasone at the Williamsburg Economic Summit in 1983. Since then it has been customary for the host country to report briefly to the Summit on the outcome of the meeting. Previous conferences in this annual series have been hosted by Japan, France, West Germany and Canada. There may be a presumption amongst other Summit States that the UK will host a conference in either 1989 or 1990. However, with the prospect of 'Warnock' legislation in train in 1989 (and quite possibly in 1990), the Prime Minister is anxious to avoid such public examination of related issues in the UK at the same time. We understand that the USA may reluctantly be prepared to host the 1989 conference. In the event that this issue arises in Paris you may like to explain our position. If there is strong

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pressure on us to take a turn we may need to reflect further on the possibility of holding a conference on some bioethical issue, though in 1990 not 1989.

4. I am copying this minute to Sir Geoffrey Littler and Rodric Braithwaite, as well as to David Tanner at the DES.

JP JOHN FAIRCLOUGH
Chief Scientific Adviser

Jane Lane.

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SHERPA MEETING: PARIS: 19-21 MAY

Human Frontier Science Programme (HFSP)

UK BRIEF

1. OBJECTIVES

1.1 Keep Japanese Government in the lead on HFSP as a Japanese initiative.

1.2 Encourage Japanese Government to put any proposals it has to make on implementing HFSP directly to other Summit Governments through the normal channels.

1.3 Maintain sympathetic interest while formally reserving UK Government's position until a proposal has been received and studied.

1.4 Keep substantive discussion of HFSP away from the Summit and Sherpa meetings; limit Summit reference at most to brief progress report for noting (only).

1.5 (Indirect) Get Japan to meet full cost of first five years.

2. LINE TO TAKE

2.1 This is an interesting, imaginative and potentially important initiative by Japan. It marks her growing strength in basic science research. We see it as an earnest of her desire, as the second wealthiest democracy, to take her place with other advanced democracies in contributing to the world's stock of basic scientific understanding. We were grateful for the opportunity offered to our scientists and science policy makers to join, on a personal basis, in some of the discussions of the Japanese Feasibility Study Committee. We understand that the Committee has now completed its report and it is submitting it to

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the Japanese Government. The UK stands ready to consider sympathetically any proposals that the Japanese Government may decide to make to other Summit countries.

2.2 At the last Summit meeting Japan made a progress report which received reference in the communique, accompanied by an expression of interest. We do not think it would be timely or appropriate to discuss at the Toronto Summit either the report of the Japanese Feasibility Study Committee, or any substantive proposals the Japanese Government may wish to make. The first item was a report to the Japanese Government, not to the Summit Governments collectively. Even if the Japanese Government has formal proposals to make to its Summit colleagues there is insufficient time to give them due consideration before the Summit; moreover the topic is not apt for substantive Summit discussion.

2.3 We would therefore encourage the Japanese Government, as and when it may have proposals to make, to communicate these in the normal way to Ministers responsible in the individual Summit countries who can then make their own responses.

2.4 However, if the Japanese Government is so minded, the Summit could receive a short[written] progress report, which could be noted.

2.5 It would not be inappropriate, if Japan so chooses, to inform the EC Commission of any proposals that it makes, on the same basis as the Commission participates in Summit. UK does not however/see the Commission playing a major part in the HFSP. It will be a matter for each Summit Government to determine its own response.

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3. BACKGROUND

3.1 The HFSP is a programme for basic science, to advance understanding of biological mechanisms in systems from the molecular level to the whole individual. While leaving the scope deliberately broad, the programme is likely to concentrate on (i) basic research for the elucidation of brain functions and (ii) basic research for the elucidation of biological functions through molecular level approaches. It is intended that through international collaboration in these fields advances in basic understanding will produce the seeds for future scientific and technological development in the next century. The main activities of the programme will be fellowships, research grants, workshops, and the collection and dissemination of information. A fairly modest start is envisaged, with the initial phase building up to perhaps 30-50 research grants a year, 100-200 fellowships a year and 10-20 workshops a year. The programme would be overseen and run by an internationally composed scientific committee drawn from Summit country participants and operating on the basis of the peer review of proposals put to them following programme announcements of the main areas of activity.

3.2 The last international meeting of the Feasibility Study Committee was convened by Japan in Bonn on 29 April. This was the fourth such meeting over the past year and was attended by Dr. V. Harrison of the MRC who had attended the previous meetings. The participants agreed a declaration (Annex 1).

3.3 The UK has made its position clear throughout. We are interested in the programme and in the possibility of collaborating. We are not in the position to contribute any funds to the programme at least for the 3-5 years. But we would be willing to offer collaboration, goodwill and contributions in

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kind were the Japanese Government to make a suitable proposal and the UK Government to agree to respond.

April 29, 1988

The Alexander von Humboldt Foundation

1. At the Bonn Wise Men's Conference, an international gathering of scientists confirmed the substantial progress made during the conduct of the Feasibility Study on the Human Frontier Science Program under Japan's leadership. The Study, conducted between November 1987 and March 1988, was successful in the sense that the scientific focus, international character and the initial level of effort required had taken substantial shape.
2. The assembled scientists were unanimous in their support of this program and were particularly encouraged by the early prospects of an initial phase. They commended the Government of Japan and its scientific leaders for taking the initiative in proposing HFSP, for continuing its promotion as well as for leading the conduct of the Feasibility Study.
3. The enthusiasm for HFSP is a reflection and a recognition of the growing internationalization of scientific research and of the appropriateness of organizing it on a global basis. Moreover, HFSP is seen not only as a means of providing funds for international collaborative science, but also for disseminating new scientific findings. Three elements would comprise the program:
 - 1) research grants in support of specific projects
 - 2) fellowships, both short and long term to enable scientific exchange
 - 3) workshops to enhance information exchange
4. Enhanced support for basic research in the life sciences is also a recognition that the tremendous progress made in the last few decades in fields such as molecular biology and neuroscience provide a powerful indication of the value of pursuing such work in a pronounced, multidisciplinary and international fashion. The results would provide the underpinnings for future scientific and technological development, which would lead to the benefit for all mankind.

5. Because studies related to the "elucidation of superior biological functions" cover such a vast territory, the Feasibility Study focussed on two aspects of biological research: the elucidation of brain functions, and the elucidation of biological functions through molecular level approaches. Also, it is extremely encouraging that HFSP will be aimed primarily at the support of young established and promising investigators and that selection process will be based on a peer review system.

6. The scientists in Bonn felt it important for the Program to be started as soon as possible, even if the scale is limited. Japan's initiative and efforts up to this point were highly appreciated and it was hoped that Japan would continue to take the initiative, including financial contributions, for the implementation of the Program at the earliest possible time. It was also expected that other summit member countries would actively strive for the promotion of the Program.

The assembled scientists expressed their commitment to the realization of HFSP and appeal to their scientific colleagues and to decision-makers in government for their collaboration and support.

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